ECONOMIC UPDATE

REGIONS

March 16, 2022

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March FOMC Meeting: A Big Thing With A Small Beginning?

- The FOMC raised the Fed funds rate target range by 25 basis points, with the mid-point of the target range rising to 0.375 percent
- The updated dot plot implies 25-basis point funds rate hikes at each remaining 2022 FOMC meeting

That the FOMC would raise the Fed funds rate target range by 25 basis points at their March meeting was as close to a given as there is. What was much more uncertain, however, is how far the FOMC would signal they would go in response to inflation expected to remain well above their 2.0 percent target rate at a time of considerable uncertainty. As it turns out, the FOMC went further than we and many others expected, with the updated dot plot implying 25-basis point hikes in the funds rate target range at each remaining 2022 meeting and further implying the FOMC will raise the funds rate above their own estimate of the neutral rate. Clearly, the Committee intended to send an aggressive signal of their resolve to rein in inflation and keep inflation expectations in check. What remains to be seen, however, is the extent to which they follow through on the aggressive signal sent at this meeting. After all, if there is one thing any of us should have learned over the past two years, it is how quickly, and how drastically, things can change.

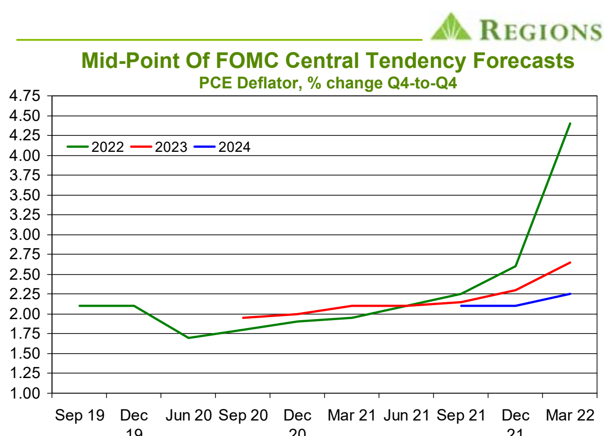
The Committee's assessment of current economic conditions notes that economic activity and employment have continued to strengthen while inflation remains elevated. The Committee also noted that the implications for the U.S. economy of Russia's invasion of Ukraine are highly uncertain, the near term implications will likely result in upward pressure on inflation while acting as a drag on economic activity. Many, us included, had thought this heightened uncertainty would lead to a less aggressive course of rate hikes than that laid out in the updated dot plot, but that proved to not be the case.

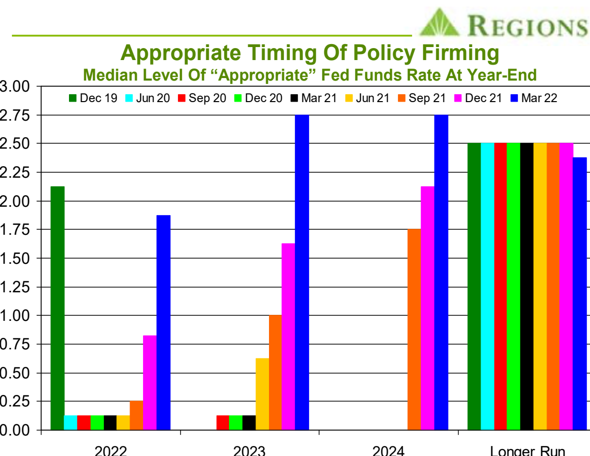
The updated economic projections show a meaningful downgrade to expected real GDP growth; on a Q4/Q4 basis, the mid-point of the central tendency forecasts now shows anticipated growth of 2.75 percent for 2022 compared to the December 2021 projection of 4.05 percent. At the same time, expected inflation is significantly higher than was the case in the December 2021 projections. The mid-point of the central tendency forecasts now shows PCE inflation running at 4.40 percent, Q4/Q4, in 2022, up from 2.60 percent in the December 2021 projections. There were also upward revisions to the forecasts for 2023 and 2024, and similar upward drifts in the projections for core PCE inflation. Indeed, on a Q4/Q4 basis, the mid-point of the central tendency forecast of core PCE inflation now stands at 2.70 percent for 2023, up from 2.25 percent in the prior projections. It is also worth noting that each of the 16 Committee members indicated they see the risks to their forecasts of headline and core inflation as weighted to the upside, which has never before happened in the life of the projections. In his post-meeting press conference, Fed Chairman Powell stated that the Committee "is attentive to the risks of further upward pressure on inflation and inflation expectations."

It could be argued that this attentiveness is reflected in the updated dot plot. The median year-end dots imply a target range mid-point of 1.875 percent for 2022 and 2.75 percent for both 2023 and 2024, with the median projection showing the Committee pushing the funds rate above their estimate of neutral. At the same time, the median estimate of the neutral funds rate fell from 2.50 percent to 2.375 percent, which stands out given that the median estimates of longer-term real GDP growth, inflation, and the unemployment rate all remained the same.

In his post-meeting press conference, Chairman Powell stated that "the way we're thinking about this is that every meeting is a live meeting and we're going to be looking at evolving conditions." Mr. Powell also held out the possibility that 50-basis point moves are not out of the question at future meetings, depending on the evolution of economic and financial conditions. Perceptions amongst market participants remain mixed; some fear the FOMC is on course for a policy mistake by not acting more aggressively to help rein in inflation, others fear the FOMC is on course for a policy mistake by acting so aggressively that they tilt the economy into recession. Those perceptions will of course evolve as conditions change. It is worth noting that St. Louis Fed President Bullard dissented in today's voting, preferring a 50-basis point funds rate hike.

It is said that big things can have small beginnings. Whether that proves to be the case with the series of Fed funds rate hikes that began today remains to be seen. About the only thing we can be sure of at this point is that it is unlikely to play out how we think today it will play out.





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